United Nations E/C.18/2013/4

Economic and Social Council

Distr.: General
9 August 2013

Original: English

Committee of Experts on International Cooperation in Tax Matters
Ninth session
Geneva, 21-25 October 2013
Items 6 (a) (v) and (b) (i) of the provisional agenda*
Discussion of substantive issues related to international cooperation in tax matters: issues related to the updating of the United Nations Model Tax Convention: article 9: associated enterprises: update of its commentary; other issues: issues for the next update of the United Nations Practical Manual on Transfer Pricing for Developing Countries

Transfer pricing issues for consideration by the Committee

Note by the Secretariat**

Introduction

1. There are two specific transfer pricing issues on the provisional agenda for the ninth annual session. First, item 6 (a) (v) is the consideration of the commentary to article 9 on associated enterprises. In essence, the present consideration is the carry-over of a brief consideration of that commentary at the seventh annual session in 2011 as part of the finalization of the United Nations Model Double Taxation Convention between Developed and Developing Countries (the United Nations Model Tax Convention).

2. This first issue involves consideration of the commentary, rather than article 9 itself, and it was agreed by the Committee in 2011 that such a discussion should await completion of the (now finalized) United Nations Practical Manual on Transfer Pricing for Developing Countries (the Manual).

3. The second issue (item 6 (b) (i)) is that of which issues should be addressed in the next update of the Manual. As noted below, some suggestions for further issues

* E/C.18/2013/1.

** The present paper was prepared by the Secretariat. It is an overview of the "state of play" solely to assist Committee consideration and does not necessarily reflect particular views on substantive issues.

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to be addressed by the Manual are contained in the Manual itself; others flow from the work in developing the Manual and from comments on it.

4. Both of the issues and options available to address them are dealt with in more detail below.

Revision of the commentary to article 9

Background to the issue

5. Revision of the commentary to article 9 is on the agenda for the ninth annual session of the Committee as a result of a decision taken at the eighth annual session in 2012. That decision was grounded in an accommodation reached by the Committee at its seventh annual session in 2011, when the issue of the commentary to article 9 was last discussed. That was in the context of the agenda item on the United Nations Model Tax Convention update, and the update was approved in that annual session. The report of the annual session (E/2011/45) notes as follows:

> *Article 9: Associated enterprises*
>
> 40. The main issue for the commentary on article 9 related to the wording in paragraph 3 of the 2001 version of the commentary expressing a recommendation by the former Group of Experts that countries should follow the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (OECD Transfer Pricing Guidelines) in applying the arm's-length principle. Paragraph 3 of the 2001 United Nations Model Convention provides:
>
> > With regard to transfer pricing of goods, technology, trademarks and services between associated enterprises and the methodologies which may be applied for determining correct prices where transfers have been made on other than arm's-length terms, the Contracting States will follow the OECD principles which are set out in the OECD Transfer Pricing Guidelines. These conclusions represent internationally agreed principles and the Group of Experts recommend[s] that the Guidelines should be followed for the application of the arm's-length principle which underlies the article.
>
> 41. Following discussion, it was agreed to retain the existing paragraph, which endorsed the arm's-length principle in determining transfer pricing issues implicit in article 9 and which recognized the role that the OECD Transfer Pricing Guidelines played in practice in applying the arm's-length principle. Most members considered that those views were still appropriate. Some members raised concerns, however, about the appropriateness of the views of the former Group of Experts as set out in paragraph 3 and questioned whether they were too broadly stated. In particular, the recommendation that countries should follow the OECD Guidelines might need to mention the fact that they were only for guidance in applying the arm's-length principle. Three members (Marcos Valadão, Tizhong Liao and Anita Kapur) had reservations on the views expressed by the former Group of Experts as stated in paragraph 3 of the commentary.
>
> 42. It was agreed to consider those issues further without prejudging the outcome of such consideration. In the meantime, paragraph 3 was amended to

clarify that the views expressed by the Group of Experts in the 2001 United Nations Model Convention had not been fully considered by the Committee, although there was unanimity among the Committee members that the arm's-length principle underlay article 9 of the United Nations Model Convention. The Committee noted that work was continuing on producing a manual on the practical aspects of transfer pricing, which would focus on the issues facing developing countries. The mandate for the Subcommittee charged with that work was reconfirmed. The Subcommittee was mandated to develop a practical manual on transfer pricing, based on the following principles:

(a) It should reflect the operation of article 9 of the United Nations Model Convention, and the arm's-length principle embodied in it, and be consistent with relevant commentaries of the United Nations Model Convention;

(b) It should reflect the realities for developing countries at the relevant stages of their capacity development;

(c) Special attention should be paid to the experience of other developing countries;

(d) It should draw upon the work being done in other forums.

43. In addition, it was confirmed that the work would continue in accordance with the understandings outlined in paragraph 48 of the report on the sixth session (E/2010/45), including that it would be consistent with the OECD Transfer Pricing Guidelines, to which the United Nations commentaries made reference.

44. In accordance with the results of the discussions as noted, it was agreed that the wording of paragraph 3 should be amended to read as follows (the new wording is in boldface type):

> With regard to transfer pricing of goods, technology, trademarks and services between associated enterprises and the methodologies which may be applied for determining correct prices where transfers have been made on other than arm's-length terms **the former Group of Experts stated that** the contracting States will follow the OECD principles, which are set out in the OECD Transfer Pricing Guidelines. **The former Group of Experts, in the United Nations Model Convention published in 2001, came to the view that** these conclusions represent internationally agreed principles and **it** recommend**ed** that the Guidelines should be followed for the application of the arm's-length principle which underlies the article.
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> **The views expressed by the former Group of Experts have not yet been considered fully by the Committee of Experts, as indicated in the records of its annual sessions.**

Matters for consideration in relation to the commentary

6. As noted, the further consideration of paragraph 3 was in effect deferred until after the Manual was completed. Now that completion has been achieved, the issues for the Committee include:

(a) Whether the consideration should be confined to that of paragraph 3 or should include a broader review of the article 9 commentary;

(b) The priority that should be accorded to the present work and its particular elements;

(c) The relationship to work being conducted by other organizations and entities;

(d) Whether a subcommittee should be formed to consider the issues, and if so whether it should also be responsible for work on updating the Manual (considered below);

(e) The extent to which any such subcommittee should be asked in its mandate to consider certain issues, while leaving available the option for the subcommittee to recommend other such issues for consideration;

(f) The Coordinator for any such subcommittee (traditionally chosen from among members of the Committee, when possible);

(g) The extent to which the membership of any such subcommittee should be determined at the annual session, could be agreed upon later or could be left to the discretion of the Coordinator, bearing in mind the need for broad and balanced representation in practical terms;

(h) The need for different subcommittees to consult on issues that have obvious "cross-cutting" aspects.

Update of the Manual

7. The Manual was finalized at the eighth session in October 2012, subject to some minor editing. The Manual was officially launched on 29 May 2013 after completion of that editing. The Manual notes that some issues should be part of the next edition. Paragraph 6.3.5 provides examples of the application of the transactional net margin method, and footnote 60 to the paragraph reads:

> The examples below derive from the US Internal Revenue Service Intercompany Transfer Pricing Regulations. The Manual will include examples from developing countries in the next edition.

8. The need for more developing country examples is a general one, consistent with the mandate for the Manual that special attention should be paid to the experience of other developing countries.

9. Paragraph 6.1.2.7 gives only a brief discussion of intangibles, and footnote 53 to this discussion says:

> The Subcommittee discussed the possibility of preparing more detailed guidance on intangibles in a separate Chapter of this Manual, but was unable to complete the work in the time available. This item will be added to the programme of work with a view for completion for the next edition of the Manual.

10. Finally the Manual notes, at paragraph 8.2.2.8, in respect of capacity-building programmes in transfer pricing that:

> These programmes are many and varied in content but are essentially aimed at bringing international expertise and best practice to countries in need of developing and furthering their transfer pricing regimes. The next edition of this Manual is expected to include a list of available training resources and advice on accessing them.

11. The paper presented to the annual session for comment in 2012, entitled "Transfer pricing: technical assistance and capacity building resources" (E/C.18/2012/CRP.14) is a potential basis for such a chapter.

12. Another issue not addressed in any detail in the Manual, but where work has already been done in the subcommittee, is that of intra-group services.

13. In his final report for the Committee in October 2012 (E/C.18/2012/CRP.1), Stig Sollund, Coordinator of the Transfer Pricing Committee, touched upon some of those issues when he noted in paragraphs 6 to 8 that:

> It has become clear, however, that the Manual would benefit from further, more detailed, examination of issues such as the treatment of intangibles and services. Not all users of the Manual will seek such additional detail, but many will, reflecting the fact that developing countries are at many different stages on their respective transfer pricing "journeys".
>
> This further elaboration would represent a natural "Phase 2" of the Manual's life, rather than a current incompleteness, and the Committee may wish to consider providing the Subcommittee with a mandate to continue work on such more detailed examination of relevant issues, and on making proposals for the updating and continuous improvement of the Manual, with an initial view to putting forward proposals to the ninth annual session of the Committee in 2013. This will only improve the Manual's relevance to users and its significance as a work that can be relied upon in the capacity-building efforts of the United Nations and others that are so needed in this field.
>
> The Secretariat has also commissioned a report on training opportunities available in the area of Transfer Pricing. This will be made available to the Committee separately with a view to its being transformed into an Annex to the Manual.

14. In the report of its eighth annual session (E/2012/45, para. 20), the Committee noted that:

> Issues that could not be addressed at the present stage would be collected by Mr. Sollund until 30 June 2013 and included in a catalogue of items to be handed over to the new membership of the Committee for future discussion and possible inclusion in later editions.

15. That catalogue of items, which is not expected to be lengthy, will be available before the ninth annual session as document E/C.18/2013/CRP.15.

Matters for consideration in relation to the Manual

16. The matters for the Committee in relation to the updating of the Manual as a "living document" include:

(a) The priority that should be accorded to the present work and its particular elements;

(b) Whether a subcommittee should be formed to consider the issues, and if so whether it should also address the revision of the commentary on article 9 (considered above);

(c) The relationship to work being conducted by other organizations and entities;

(d) The extent to which any such subcommittee should be asked in its mandate to consider certain issues, while leaving available the option for the subcommittee to recommend other such issues for consideration;

(e) The Coordinator for any such subcommittee (traditionally chosen from among members of the Committee, when possible);

(f) The extent to which the membership of any such subcommittee should be determined at the annual session, or could be agreed upon later or could be left to the discretion of the Coordinator, bearing in mind the need for broad and balanced representation in practical terms;

(g) The need for different subcommittees to consult on issues that have obvious "cross-cutting" aspects.